No. 15-233

IN THE

Supreme Court of the United States

THE COMMONWEALTH OF PUERTO RICO, ALEJANDRO GARCÍA PADILLA, as Governor of the Commonwealth of Puerto Rico, and CÉSAR MIRANDA RODRÍGUEZ, as Secretary of Justice of the Commonwealth of Puerto Rico,

Petitioners,

v.

FRANKLIN CALIFORNIA TAX-FREE TRUST, *et al.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the First Circuit

REPLY BRIEF FOR PETITIONERS

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March 14, 2016

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

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INTRODUCTION

Respondents' argument boils down to the proposition that Congress has stripped Puerto Rico of access to *any* legal mechanism to restructure its public utilities' debts. That argument is both implausible and incorrect. Those public utilities provide such essential services as electricity. They now face an unprecedented fiscal crisis, and cannot all repay their debts in full while continuing to provide such services. Municipal bankruptcy law exists precisely to address such a crisis by creating a mechanism for such entities to restructure their debts in a way that is fair not only to their creditors, but also to the people they serve. This Court should not lightly assume that Congress—"without fanfare or even (so far as the history shows) a fight," BlueMountain Br. 2—took the momentous step of leaving Puerto Rico's public utilities, and the 3.5 million people they serve, at the mercy of their creditors.

According to respondents, Congress took that step in 1984 by defining the word "State" in the federal Bankruptcy Code. In their view, that definition "exclude[s] Puerto Rico ... from eligibility for Chapter 9," Franklin Br. 24, while leaving Puerto Rico subject to Chapter 9 preemption. But there is no reason to suppose that Congress intended Chapter 9's preemptive scope to exceed its remedial scope. To the contrary, by excluding Puerto Rico from the definition of "State" "for purpose of defining who may be a debtor under chapter 9," Congress removed Puerto Rico from Chapter 9's scope altogether. The only role a "State" plays in the Chapter 9 regime is to authorize its municipalities to access Chapter 9.

Because Puerto Rico is not a "State" eligible to authorize its municipalities to access Chapter 9, there is no reason to suppose that Congress intended for Puerto Rico to be a "State" under Chapter 9.

Indeed, respondents are unable to identify *any* way in which, under the current definition of "State," Chapter 9 could apply to Puerto Rico. They do not seriously suggest that Section 903, which limits the effect of Chapter 9 on state law, applies to a jurisdiction, like Puerto Rico, categorically beyond the scope of Chapter 9. Nonetheless, they insist that Section 903(1), a proviso that in turn limits Section 903, preempts Puerto Rico's municipal bankruptcy law. But that interpretation turns the statute's structure on its head, with the proviso sweeping far more broadly than the principal clause it modifies. Respondents suggest no reason why Congress, without explanation, would have engaged in such idiosyncratic drafting with such far-reaching and dire consequences for Puerto Rico.

Respondents' interpretation also contravenes background legal presumptions, which respondents dismiss as "dice-loading principles." BlueMountain Br. 41. But this Court has "loaded the dice" for a reason: to prevent statutes from being interpreted, as respondents propose, in ways that threaten underlying constitutional values.

At bottom, respondents identify nothing in the statutory text, structure, or history to suggest that Congress intended to preclude Puerto Rico from access to *any* legal mechanism to restructure its public utilities' debts. Accordingly, this Court should reverse the judgment.

ARGUMENT

I. Section 903(1) Does Not Preempt The Recovery Act.

A. By Its Plain Terms, Section 903(1) Does Not Apply To Puerto Rico.

Respondents argue that "[t]he Recovery Act falls squarely within Section 903(1)'s text" because "[i]t is a 'State law' prescribing a method for binding creditors without their consent." BlueMountain Br. 16 (quoting 11 U.S.C. § 903(1)); *see also id.* at 18-19; Franklin Br. 1-2, 7-8. But that argument assumes that the word "State" in Section 903(1) encompasses Puerto Rico. Obviously, Puerto Rico is not one of the fifty States. Whether Puerto Rico qualifies as a "State" within the meaning of any particular provision of federal law is a question of statutory interpretation that hinges on Congress' intent in drafting that provision. *See, e.g.*, *Examining Bd. of Eng'rs, Architects & Surveyors v. Flores de Otero*, 426 U.S. 572, 580-81 & n.10 (1976); *Calero-Toledo v. Pearson Yacht Leasing Co.*, 416 U.S. 663, 670-76 (1974); *Córdova & Simonpietri Ins. Agency, Inc. v. Chase Manhattan Bank, N.A.*, 649 F.2d 36, 38 (1st Cir. 1981) (Breyer, J.).

Respondents insist that Puerto Rico is a "State" within the meaning of Section 903(1) because the federal Bankruptcy Code defines "State" to "include[] ... Puerto Rico, except for the purpose of defining who may be a debtor under chapter 9." 11 U.S.C. § 101(52), Pet. App. 273a. Because Section 903(1) does not "defin[e] who may be a debtor under chapter 9," they assert, Puerto Rico's Recovery Act is a "State" law under Section 903(1), even though Puerto Rico is categorically ineligible to authorize its

municipalities to seek relief under Chapter 9 in the first place. *See* BlueMountain Br. 18, 25; Franklin Br. 8, 15, 18-19, 24-25.

But it is nonsensical to interpret the word "State" in Chapter 9 to include Puerto Rico where Congress expressly excluded Puerto Rico from the definition of "State" "for the purpose of defining who may be a debtor under chapter 9." 11 U.S.C. § 101(52), Pet. App. 273a. "[D]efining who may be debtor under chapter 9," *id.*, is the *only* role a "State" plays in the Chapter 9 regime, *see* 11 U.S.C. § 109(c)(2), Pet. App. 274-75a. Thus, by precluding Puerto Rico from authorizing its municipalities to seek relief under Chapter 9, Congress removed Puerto Rico from the scope of Chapter 9.

It is no answer to say that "[h]ad Congress meant to exempt Puerto Rico ... from Section 903(1), it easily could have written § 101(52) to exclude Puerto Rico as a State 'with respect to all provisions in Chapter 9,' instead of merely excluding them 'for the purpose of defining who may be a debtor' in Chapter 9." Franklin Br. 25; *see also* Pet. App. 99a. That approach would have left Puerto Rico's municipalities eligible to be debtors under Chapter 9, because eligibility for Chapter 9—like the Code's other substantive chapters—is governed by Chapter 1, the Code's "General Provisions" section. *See* 11 U.S.C. § 109, Pet. App. 273-79a ("Who may be a debtor"). Thus, excluding Puerto Rico from the definition of "State" in Chapter 9 would have left Puerto Rico free under Section 109(c) to authorize its municipalities to access Chapter 9. Only by excluding Puerto Rico from the scope of "State" in

Section 109(c) could Congress exclude Puerto Rico from the entire Chapter 9 regime.

Indeed, respondents are unable to identify any way in which, after the 1984 amendment, Chapter 9 could apply to Puerto Rico. The word "State" appears just three times in that Chapter: twice in Section 903 and once in its proviso, Section 903(1). Section 903 specifies that the federal Chapter 9 regime "does not limit or impair" a State's control over its municipalities. *See* 11 U.S.C. § 903, Pet. App. 279a. That rule has no legal or logical application to a jurisdiction, like Puerto Rico, that Congress has categorically excluded from the Chapter 9 regime. Thus, in over one hundred pages of briefing, respondents offer no interpretation of Section 903 that could apply to Puerto Rico.[1]

Respondents insist that "[e]ven if Section 903's first clause were inapplicable, ... that would not render Section 903(1)'s preemption clause irrelevant." BlueMountain Br. 30; *see also* Franklin Br. 20. But that argument ignores the statute's structure. Contrary to respondents' assertion, Section 903(1) is not "an independent rule of law."

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[1] Their only effort on this score comes in a passing footnote. *See* BlueMountain Br. 30 n.5 ("Although Congress certainly *could* (given its broad power over Territories) 'limit or impair' (11 U.S.C. § 903) Territories' control over their municipalities, Section 903's opening clause makes clear that *Chapter 9* does not do so.") (emphasis in original). Congress' constitutional power over the Territories, however, has no bearing on the statutory issue presented here. Because Section 903 is a limitation on Chapter 9, it cannot apply to a jurisdiction (like Puerto Rico) that Congress has categorically excluded from the scope of Chapter 9.

BlueMountain Br. 31; *see also* Franklin Br. 20. By its terms, it is a limitation on Section 903, which itself is a limitation on Chapter 9. Because Chapter 9 does not apply to Puerto Rico, it follows that Section 903 does not apply to Puerto Rico, and hence that Section 903(1) does not apply to Puerto Rico.

Not surprisingly, respondents devote considerable efforts to trying to divorce Section 903(1) from Section 903. In particular, they assert that "[a] proviso does not necessarily carve out an exception to the preceding clause; indeed, provisos are frequently used to 'state a general, independent rule.'" BlueMountain Br. 30 (emphasis omitted; quoting *Republic of Iraq v. Beaty*, 556 U.S. 848, 858 (2009)); *see also* Franklin Br. 20-21. But that assertion confuses the exception with the rule. As the very case cited by respondents confirms, "the 'general office of a proviso is to except something from the enacting clause, or to qualify and restrain its generality.'" *Beaty*, 556 U.S. at 858 (quoting *United States v. Morrow*, 266 U.S. 531, 534 (1925)).

While that rule is not ironclad, *see id.*, there is no reason to suppose that Congress deviated from it here. Respondents argue that "it would make no sense to read Section 903(1) as an exception to the main clause of Section 903, since the two clauses deal with different subjects." Franklin Br. 21; *see also* BlueMountain Br. 31 ("Section 903(1) ... does not create an exception to the rule that States may control their municipalities; it makes a federal regime Congress enacted pursuant to its bankruptcy power exclusive."). That argument is mystifying. Sections 903 and 903(1) address precisely the same subject: the extent to which Chapter 9 "limit[s] or

impair[s] the power of a State to control ... a municipality of or in such State." 11 U.S.C. § 903, Pet. App. 279a. Section 903 provides that Chapter 9 imposes no such limits, *see id.*, while Section 903(1) qualifies that rule by barring covered States from prescribing a method of composition of their municipalities' debts that binds nonconsenting creditors, *see* 11 U.S.C. § 903(1), Pet. App. 279a. Far from being "independent" of Section 903, Section 903(1) cannot be read apart from Section 903 in light of its textual reference ("such municipality") back to Section 903. Indeed, until 1978, Section 903(1) was not even located in a separate subsection; it was joined to the principal clause by the words "*Provided, however*." JA571, 581, 598.[2]

Respondents themselves underscore this relationship by emphasizing that Section 903(1) "was enacted to overrule *Faitoute Iron & Steel Co. v. City of Asbury Park*, 316 U.S. 502 (1942)." Franklin Br. 9. *Faitoute* relied on Section 903's precursor to hold that Chapter 9 did not preempt a state municipal restructuring law. *See* 316 U.S. at 508-09. As respondents put it, "[b]ecause *Faitoute* had relied on Section 83(i) [Section 903's precursor] to support its

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[2] Unsurprisingly, the Franklin respondents' counsel of record acknowledged long before this litigation was contemplated that "[Section 903(1)] appears *as an exception* to § 903's respect for state law in chapter 9." Thomas Moers Mayer, *State Sovereignty, State Bankruptcy, & A Reconsideration of Chapter 9*, 85 Am. Bankr. L.J. 363, 379 n.84 (2011) (emphasis added). That is certainly a far cry from the Franklin respondents' current assertion that "it would make no sense to read Section 903(1) *as an exception* to the main clause of Section 903." Franklin Br. 21 (emphasis added).

non-preemption holding, it was natural for Congress to overrule *Faitoute* by amending Section 83(i), thereby addressing in one place *both the area of autonomy preserved to the states and the new proscription on state conduct*." Franklin Br. 22 (emphasis added). Section 903(1), in other words, was designed to take away some of what Section 903 preserves. But insofar as Section 903 preserves nothing for Puerto Rico, Section 903(1) takes away nothing from Puerto Rico.

Because respondents cannot identify any way in which Chapter 9 applies to Puerto Rico, they argue that its applicability *vel non* to Puerto Rico is irrelevant. In their view, petitioners "confuse[] whether Chapter 9 governs the Commonwealth's municipalities with the separate question whether Chapter 9 affords them relief." BlueMountain Br. 26 (emphasis omitted).

But notice the critical shift in the subject matter of respondents' argument. They try to deflect the focus from *Puerto Rico* to Puerto Rico's *municipalities*. That distinction matters because the question here is whether, after the 1984 amendment, the word "State" in Chapter 9 encompasses Puerto Rico (as opposed to its municipalities). Petitioners' point, as noted above, is that it makes no sense to interpret the word "State" in that context to include a jurisdiction, like Puerto Rico, that Congress has removed from the scope of Chapter 9.

It is no mystery why respondents wish to discuss Puerto Rico's municipalities rather than Puerto Rico itself. That semantic sleight-of-hand allows them to play what they apparently view as their trump card: the argument that Puerto Rico's municipalities are

indistinguishable, for Chapter 9 purposes, from the municipalities of States that have not specifically authorized those municipalities to pursue Chapter 9 relief (or municipalities ineligible to pursue Chapter 9 relief for any other reason). *See* BlueMountain Br. 2-3, 17, 26-27, 31-33; Franklin Br. 19-20 & n.6. As they put it, "[i]f the Commonwealth *municipalities'* ineligibility to invoke Chapter 9 exempted *them* (as petitioners claim) from Section 903(1), the same would be true of *municipalities* in every State that has taken Chapter 9 off the table." BlueMountain Br. 32 (emphasis modified).

In respondents' view, in other words, the relevant comparison here is between *municipalities* eligible and ineligible for Chapter 9 relief. Under this view, San Juan (or PREPA) is no differently situated than Boston, because Massachusetts has not "specifically authorized" its municipalities to pursue Chapter 9 relief.

But that misses the point. The question here is whether the word "State" in Chapter 9 includes Puerto Rico. Whether any particular municipality meets any or all of the eligibility criteria for Chapter 9 has nothing to do with the answer to that question. Thus, the relevant comparison is not between Puerto Rico's municipalities and Massachusetts' municipalities, but between Puerto Rico and Massachusetts. And those jurisdictions are not similarly situated: Congress has specifically precluded Puerto Rico, unlike Massachusetts, from authorizing its municipalities to access Chapter 9. Massachusetts is free, at any time, to authorize its municipalities to seek relief under Chapter 9, regardless of whether it has done so to date. Thus,

no one would suggest that Massachusetts is outside the scope of Chapter 9, while the same cannot be said of Puerto Rico.[3]

Nor is there anything "far-fetched" about Congress' decision to treat Puerto Rico (and the District of Columbia) differently than the States for Chapter 9 preemption purposes. Franklin Br. 6; *see also* BlueMountain Br. 2. Indeed, the definition of "State" in the 1984 amendment puts Puerto Rico and the District of Columbia in the same position for Chapter 9 purposes as other non-State jurisdictions (the Virgin Islands, Guam, and the Northern Mariana Islands). These jurisdictions are not covered by the definition of "State" in Section 101(52) for any purposes, so as a textual matter they are beyond both the remedial and the preemptive scope of Chapter 9. *See* Comm. Br. 53 n.4. Respondents' argument that Congress would not have treated Puerto Rico and the District of Columbia differently from the States for preemption purposes notably fails to address these other jurisdictions.

In any event, this Court has long held that the Bankruptcy Code does *not* preempt state laws

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[3] Because Puerto Rico is differently situated from the States for Chapter 9 purposes, there is no merit to the suggestion of petitioners' *amicus* Association of Financial Guaranty Insurers (AFGI) that accepting petitioners' position "would cause immeasurable and unjustified harm to the nation's $4 trillion municipal bond market." AFGI Br. 9. As explained in the text, petitioners' position does not lead to the "logical and inescapable conclusion" that "all States and territories [may] enact municipal bankruptcy laws inconsistent with the Chapter 9 system." *Id.* at 8-9. In any event, this is a statutory case, and AFGI always may ask Congress to amend the statute.

governing the restructuring of entities, like insurance companies and banks, excluded from the Code. *See, e.g.*, *Neblett v. Carpenter*, 305 U.S. 297, 303-05 (1938); *Doty v. Love*, 295 U.S. 64, 70-74 (1935). To allow state law to fill the gap left by an exclusion from federal law, in short, is not to "nullify" the exclusion. Franklin Br. 6.

B. Neither Statutory History Nor Purpose Suggests That Section 903(1) Applies To Puerto Rico.

Just as respondents' textual arguments miss the mark, so too do their arguments based on Section 903(1)'s history and purpose. None of those arguments relates in any way to the critical issue here: the effect of the 1984 amendment excluding Puerto Rico from the definition of "State" "for the purpose of defining who may be a debtor under chapter 9 of this title." 11 U.S.C. § 101(52), Pet. App. 273a.

Respondents argue that the history of Section 903(1) is relevant because the 1984 amendment "made no change to the text of Section 903." Franklin Br. 14. But Congress can change a statutory provision's scope as much by defining one of its terms as by altering its text.

That simple point renders irrelevant much of respondents' briefs, which focus on the history of Section 903(1). *See* Franklin Br. 1-2, 9-12, 27-28; BlueMountain Br. 8-9, 19-23. In particular, respondents deem it highly relevant that, when Congress enacted Section 903(1) in 1946, the definition of "State" in the Bankruptcy Code included Puerto Rico. *See* BlueMountain Br. 22; Franklin Br. 13-14. At that time, everyone agrees, Puerto Rico

(like the States) could authorize its municipalities to seek relief under Chapter 9, and was thus encompassed within the meaning of the word "State" in Chapter 9. In respondents' view, there is no reason to suppose that Congress departed from that understanding when it added a new definition of "State" (which had been missing from the Code since 1978) in 1984. *See* BlueMountain Br. 24; Franklin Br. 13-15.

But that is a *non sequitur*. When Congress added a new definition of "State" to the Bankruptcy Code in 1984, it broke with past practice by specifically excluding a jurisdiction from that definition for the first time. In particular, since the enactment of the first version of Chapter 9 in 1934, Congress had never foreclosed *any* jurisdiction from authorizing its municipalities to access the federal restructuring regime. By foreclosing Puerto Rico from doing so in 1984, Congress took an unprecedented and (as this case underscores) far-reaching step. Although there is not one word in the legislative history to explain that step, it represented—for Puerto Rico at least—a "major change" in federal bankruptcy law. BlueMountain Br. 36 (internal quotation omitted); Franklin Br. 4, 15-16. Thus, contrary to respondents' suggestion, Congress' exclusion of Puerto Rico from the scope of Chapter 9 is not an elephant hiding in a mousehole. *See* BlueMountain Br. 24 (citing *Whitman v. American Trucking Ass'ns*, 531 U.S. 457, 468 (2001)); Franklin Br. 15-16. Rather, this elephant comes as an elephant. *Cf. Morrison v. Olson*, 487 U.S. 654, 699 (1988) (Scalia, J., dissenting).

Respondents fare no better by arguing statutory purpose. In their view, "the express purpose" of Section 903(1) is to "ensur[e] that 'only under a Federal law should a creditor be forced to accept ... an adjustment without his consent.'" Franklin Br. 2 (quoting H.R. Rep. No. 79-2246, at 4 (1946), JA411); *see also id.* at 9-10; BlueMountain Br. 21. But the legislative history on which they base that argument predates the enactment of the 1984 amendment by almost forty years. At the time that legislative history was written, there was complete symmetry between the remedial and preemptive scope of Chapter 9: every jurisdiction subject to preemption could authorize its municipalities to seek relief under Chapter 9. Respondents identify not one word in the legislative history to suggest that Congress intended the preemption provision to apply to a jurisdiction, like Puerto Rico, beyond Chapter 9's remedial scope.

Respondents' invocation of a federal purpose of ensuring bankruptcy uniformity rings equally hollow. In their view, "the whole point of Section 903(1) was to prevent States and Territories from enacting their own municipal-bankruptcy codes, which would destroy the uniformity vital to the national municipal-debt market." BlueMountain Br. 31 (emphasis omitted). But Congress itself shattered the uniformity of federal municipal-bankruptcy law by excluding Puerto Rico from the scope of Chapter 9 in the first place. Because even respondents cannot deny that federal municipal-bankruptcy law is *not* uniform with respect to Puerto Rico, their invocation of uniformity is, to say the least, ironic.

Equally unavailing is respondents' theory that Congress excluded Puerto Rico from the definition of

"State" to "*retain* jurisdiction over the restructuring of Puerto Rico ... municipal debt." Franklin Br. 5 (emphasis added); *see also id.* at 45; BlueMountain Br. 28. That theory is both factually and legally baseless. *See* Pet. App. 53a (Torruella, J., concurring in the judgment) (dismissing theory as "pure fiction"). Congress has no need to "retain jurisdiction" over Puerto Rico's municipalities to control their access to federal bankruptcy law, because Congress may grant or prohibit such access at any time. And Congress has not been in the business of governing Puerto Rico's municipalities for more than a century, when it first established a civil government for the island. *See* Ch. 191, 56th Cong., 1st Sess., 31 Stat. 77 (1900). Indeed, Congress "relinquished its control over the organization of the local affairs of the island," including its municipalities, upon the adoption of the Puerto Rico Constitution and the establishment of the Commonwealth in 1952. *Flores de Otero*, 426 U.S. at 597; *see also Calero-Toledo*, 416 U.S. at 671-74; *Córdova*, 649 F.2d at 38-41. Thus, before the 1984 amendment, Puerto Rico's Legislative Assembly—not Congress—had the power to authorize Puerto Rico's municipalities to access Chapter 9.[4]

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[4] Respondents miss the point by arguing that "'the apt analogy to the relationship between municipal and state governments is to be found in the relationship between the government of a Territory and the Government of the United States.'" BlueMountain Br. 28 (quoting *Waller v. Florida*, 397 U.S. 387, 393 (1970)); *see also* Franklin Br. 51-52. That argument would at most support the theory—which has been incorrect since at least 1952—that Congress' relationship with *Puerto Rico* is

C. Background Presumptions Confirm That Section 903(1) Does Not Apply To Puerto Rico.

Background presumptions only confirm that there is no basis to interpret Section 903(1) to apply to a jurisdiction, like Puerto Rico, that Congress has categorically excluded from the scope of Chapter 9.

1. Presumption Against Preemption

Although Puerto Rico is not a State, this Court has recognized (and respondents do not dispute) that the test for federal preemption of Puerto Rico law is "the same as" the test for state law. *Puerto Rico Dep't of Consumer Affairs v. Isla Petroleum Corp.*, 485 U.S. 495, 499 (1988). Respondents deny that the presumption against preemption applies here, however, because "[t]he federal government has a unique and powerful interest in uniform bankruptcy laws," and "there is a history of significant federal presence in the field of bankruptcy generally." BlueMountain Br. 46, 48 (internal quotation omitted); *see also* Franklin Br. 45. These platitudes simply ignore the compelling federalism interests at stake.

As an initial matter, as noted above, this case arises as a result of Congress' *deviation* from uniform federal bankruptcy laws by excluding Puerto Rico from the scope of Chapter 9. Moreover, application of the presumption against preemption "does not rely

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analogous to a State's relationship with its own municipalities. In no way does that argument support respondents' assertion that Congress' relationship with *Puerto Rico's municipalities* is analogous to a State's relationship with its own municipalities.

on the absence of federal regulation," *Wyeth v. Levine*, 555 U.S. 555, 565 (2009), and indeed courts have applied a "strong presumption against inferring Congressional preemption in the bankruptcy context" specifically, *Integrated Solutions, Inc. v. Service Support Specialties, Inc.*, 124 F.3d 487, 493 (3d Cir. 1997); *see also PG&E Co. v. California*, 350 F.3d 932, 943 (9th Cir. 2003). In any event, respondents are asking this Court to interpret a federal statute to preempt not the Commonwealth's regulation of *its citizens*, but the Commonwealth's regulation of *itself*. As this Court recognized in *Faitoute*, federal regulation of a State's "fiscal management of its own household," 316 U.S. at 509, intrudes into a core area of state concern.

Respondents insist, however, that "Congress has played the dominant role in the specific area of *municipal* bankruptcy for more than seven decades, and for nearly all of that period, federal law has been exclusive." BlueMountain Br. 47 (emphasis modified); *see also* Franklin Br. 45. But that argument glosses over this Court's cases on the validity and scope of federal municipal bankruptcy law. Far from suggesting that this is an exclusive federal field, those cases underscore just the opposite: that this is a constitutionally sensitive area in which the Federal Government must "walk[] on tiptoes." BlueMountain Br. 47; *see Ashton v. Cameron Cty. Water Imp. Dist. No. 1*, 298 U.S. 513, 529-32 (1936); *United States v. Bekins*, 304 U.S. 27, 51 (1938); *Faitoute*, 316 U.S. at 509. Congress' subsequent enactment of Section 903(1)—the constitutionality of which this Court has never addressed—in no way diminishes those underlying federalism concerns.

Respondents also deny that this Court should avoid construing the statute to create a "no man's land" governed by neither federal nor state law. *See* BlueMountain Br. 49-51; Franklin Br. 45-50. In their view, "[t]here is no established rule, and no reason, that the scope of federal preemption should be read narrowly unless Congress has supplied standards of its own." BlueMountain Br. 49. To the contrary, respondents assert, "[t]his Court has not hesitated to hold State laws preempted where Congress has decided to *deregulate* a field." *Id.* at 50 (emphasis in original).

When a court concludes that "Congress has decided to *deregulate* a field," however, it has already resolved the question of congressional intent. Here, of course, there is no indication that Congress intended to "deregulate" the field of municipal bankruptcy. Respondents' interpretation of congressional intent is simply implausible: this Court should not lightly conclude that Congress intended an unexplained exclusion from federal law to displace Commonwealth law, and thereby to deprive Puerto Rico of access to *any* legal mechanism to restructure its public utilities' debts. *Cf. Neblett*, 305 U.S. at 303-05; *Doty*, 295 U.S. at 70-74.

In addition, respondents insist that their interpretation would not leave Puerto Rico in a no man's land. That is so, they declare, because Puerto Rico's municipalities can restructure their debts (1) "through a receivership," or (2) "through negotiations with creditors." Franklin Br. 46-47. They are wrong on both scores.

As to the first: a receiver can do no more than "step[] into [the debtor's] shoes," *O'Melveny & Myers*

v. FDIC, 512 U.S. 79, 86 (1994) (internal quotation omitted), and cannot force any creditor to accept a diminished recovery for the greater good of all. *See* P.R. Laws Ann. tit. 22 § 207(e) ("[T]he powers of any such receiver shall be limited to the operation and maintenance of such undertakings, and the collection and application of the income and revenues therefrom"). Nor can a receiver "keep the lights on," Franklin Br. 59, if suppliers refuse to extend credit or deliver fuel or other goods and services, or if there is no money to pay for fuel and other operating expenses, *see, e.g.*, Br. of *Amicus* ScotiaBank de Puerto Rico 4 (characterizing repayment of fuel-line obligations as an operating expense).

As to the second: a consensual deal with creditors would be ideal if possible, but bankruptcy laws exist in part because of the collective action problems inherent in this situation. *See* Pet. App. 10a n.6. This case proves the point: PREPA has been negotiating with its creditors for a year and a half to try to work out a consensual deal. But such a deal would require, among other things, the assent of bondholders holding more than $2 billion of debt who are not at the table now. *See* Statement of Lisa J. Donahue, PREPA Chief Restructuring Officer (Jan. 12, 2016), *available at* http://tinyurl.com/jkmar38 (last visited Mar. 14, 2016).[5] The bankruptcy laws

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[5] In addition, the proposed deal requires the satisfaction of numerous other "Conditions Precedent" by June 30, 2016 including: (1) the successful resolution of any and all lawsuits—and "any appeals therefrom"—challenging the validity of the recent Puerto Rico Revitalization Act, 2016 P.R. Laws Act No. 4, and the new bonds authorized thereby, *see* PREPA Public Disclosure, Annex D at 3; Schedule I-A § 5(c), (f); Schedule I-B

exist precisely to address this "holdout" problem and force recalcitrant creditors to the table where, under judicial supervision, unpayable debts can be restructured for the greater good of all.

2. Presumption Against Raising Serious Constitutional Questions

Respondents give short shrift to the constitutional concerns surrounding Section 903(1), suggesting that "even as to States" that provision "presents no constitutional problem." BlueMountain Br. 42. In their view, Section 903(1) is necessarily valid as "an exercise of a 'power' the Constitution ... delegate[d] to Congress" in the Bankruptcy Clause. *Id.*

That argument again ignores this Court's decisions in *Ashton*, *Bekins*, and *Faitoute*. Those cases recognize that Chapter 9 raises substantial federalism concerns insofar as it permits a municipality—*i.e.*, a "political subdivision or public agency or instrumentality of a State," 11 U.S.C. § 101(40), Pet. App. 272a—to restructure its debts under federal law. Indeed, *Ashton* invalidated the original Chapter 9 on these grounds. *See* 298 U.S. at 529-32. When *Bekins* later upheld a revised version of Chapter 9, it did so only upon concluding that "[t]he statute is carefully drawn so as not to impinge upon the sovereignty of the State." 304 U.S. at 51. In particular, *Bekins* relied on the reservation of

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at 12 (Dec. 23, 2015), *available at* http://tinyurl.com/j5wymy5 (last visited Mar. 14, 2016); (2) the receipt of an "investment grade rating" for the new bonds, *see* Schedule I-B at 3, 12; and (3) hearings on, and approval of, a new securitization charge and rate structure by the Puerto Rico Energy Commission, *see id.* § 13(b)(v)-(vii), Annex D at 3.

state power now set forth in Section 903: "[Chapter 9] 'expressly avoids any restriction on the powers of the States or their arms of government in the exercise of their sovereign rights and duties,'" and thus "'no interference with the fiscal or governmental affairs of a political subdivision is permitted.'" *Id.* (quoting H.R. Rep. No. 75-517 (1937), JA389). In light of that reservation of power, "[t]he State retains control of its fiscal affairs." *Id.* And *Faitoute* confirmed the point, noting that *Bekins* had upheld Chapter 9 "only because Congress had been 'especially solicitous to afford no ground' for the 'objection' that an exercise of federal bankruptcy over political subdivisions of the State "'might materially restrict [its] control over its fiscal affairs'" whereby states would no longer be "'free to manage their own affairs.'" 316 U.S. at 508 (quoting *Bekins*, 304 U.S. at 50).

As noted above, Section 903(1) vitiates the reservation of state power upon which this Court upheld Chapter 9, and renders a State "powerless" to regulate "problems as peculiarly local as the fiscal management of its own household," *Faitoute*, 316 U.S. at 509, through its own restructuring regime. Respondents tellingly offer no response to the leading commentators who have raised this constitutional concern. *See* Comm. Br. 39-40. And if Section 903(1) is unconstitutional as to the States, there is no basis for applying it to Puerto Rico, as there is no reason to suppose that Congress would have wanted that provision to apply *only* to Puerto Rico. *Cf.* BlueMountain Br. 45 ("Section 903(1) must mean the same thing for States and Territories alike"); *United States v. Booker*, 543 U.S. 220, 247 (2005) ("[S]everability questions ... can arise when a

legislatively unforeseen constitutional problem requires modification of a statutory provision as applied in a significant number of cases."); Adrian Vermeule, *Saving Constructions*, 85 Geo. L.J. 1945, 1950 n.26 (1997).

II. Neither The Bankruptcy Clause Nor The Federal Bankruptcy Code Preempts The Field Of Municipal Bankruptcy.

Respondents now drop any pretense that their sweeping field preemption argument is anything more than a restatement of their express-preemption argument. They do not contend that either the federal Bankruptcy Clause or the federal Bankruptcy Code, independent of Section 903(1), preempts the field of bankruptcy (or the field of municipal bankruptcy). Rather, they contend that "Congress's creation of a comprehensive federal municipal-bankruptcy regime *combined* with its enactment of Section 903(1) ousting States from the field ... demonstrates Congress's intent to occupy that field exclusively." BlueMountain Br. 54 (emphasis in original); *see also id.* at 55 ("[Section 903(1)] together with the rest of Chapter 9 shows Congress's intent to occupy the field."); Franklin Br. 5 (making field preemption argument based on Section 903(1)); *id.* at 45 (same).

In other words, respondents argue that Congress has preempted the field covered by Section 903(1). But that is no different than their express preemption argument. As this Court has explained, an express preemption clause "would be pure surplusage if Congress had intended to occupy the entire field." *Wisconsin Pub. Intervenor v. Mortier*, 501 U.S. 597, 612-13 (1991). And it is hardly

surprising that respondents have abandoned a freestanding field preemption argument, because this Court rejected precisely that argument in *Faitoute*. *See* 316 U.S. at 507-09.[6]

Thus, respondents do not take seriously their own passing suggestion that "'States may not pass or enforce laws to interfere with *or* complement the Bankruptcy Act or to provide *additional or auxiliary regulations*.'" BlueMountain Br. 55 (quoting *International Shoe Co. v. Pinkus*, 278 U.S. 261, 265 (1929)) (emphasis added by respondents). Again, that is no surprise because that suggestion—if taken at face value—cannot be squared with the venerable line of cases going back to the early nineteenth century (and reaffirmed *after Pinkus*) that the federal Bankruptcy Code does *not* preempt States from enacting their own bankruptcy laws, at least insofar as they do not conflict with federal law. *See, e.g.*, *Sturges v. Crowninshield*, 17 U.S. (4 Wheat.) 122, 193-97 (1819); *Stellwagen v. Clum*, 245 U.S. 605, 613 (1918); *Doty*, 295 U.S. at 70-74; *Neblett*, 305 U.S. at 303-05; *Faitoute*, 316 U.S. at 508-09.

Finally, respondents err by suggesting that the Contract Clause plays any role in the preemption analysis. *See* BlueMountain Br. 5, 43; Franklin Br. 26-30. Contrary to respondents' suggestion, the Contract Clause does not *per se* invalidate state

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[6] Respondents' conflict preemption argument, like their field preemption argument, is entirely derivative of their express preemption argument. Because the Recovery Act is not preempted by Section 903(1), it does not "stand[] as an obstacle to the accomplishment and execution of the full objectives of Congress." BlueMountain Br. 57 (internal quotation omitted).

municipal-bankruptcy laws. Indeed, this Court specifically rejected that argument in *Faitoute*. *See* 316 U.S. at 512-16. Even assuming a state law substantially impairs a contractual relationship, a court still must inquire whether the law reasonably advances a significant and legitimate government purpose. *See, e.g., Energy Res. Grp., Inc. v. Kansas Power & Light Co.*, 459 U.S. 400, 411-12 (1983); *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 444-47 (1934). Respondents are free to pursue their Contract Clause claims on remand, but those claims have no bearing on the resolution of the preemption issue presented here.[7]

CONCLUSION

For the foregoing reasons, this Court should reverse the judgment.

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[7] Respondents' *amicus* The United States Chamber of Commerce argues that resolving the preemption issue in petitioners' favor "would create (rather than avoid) serious constitutional questions" because it would "require a remand to the lower courts to decide the Contract Clause question." Chamber Br. 19-20. That argument misperceives the doctrine of constitutional avoidance. That doctrine provides a tool for resolving statutory issues—here, the proper interpretation of the federal Bankruptcy Code. Whether an entirely different statute, Puerto Rico's Recovery Act, comports with the Contract Clause has no bearing on that statutory issue.

Respectfully submitted,

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